MAY REVISION

Pete Wilson, Governor,
State of California

1997-98 GOVERNOR'S BUDGET

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OVERVIEW

The May Revision to Governor Wilson's January budget provides updated economic and revenue forecasts, as well as the latest caseload, enrollment, and population information for programs in the health and welfare, education, and public safety areas. It contains the latest information on state expenditures for the current and coming fiscal years, and provides the latest projections on federal actions that affect state spending.

Key Features. The principal feature of the May Revision is a two-year increase in state revenues of nearly $2.3 billion, which is the result of California's ongoing economic expansion. Under Proposition 98, approximately98 percent of this revenue will be dedicated to K-12 education and the California Community Colleges. The Governor proposes to invest these additional resources in key policy areas, which include:

- An increase of $230 million to fully fund the Governor's Class Size Reduction program at a rate of $800 per student.
- For school districts unable to further reduce class sizes because of facilities needs, the May Revision provides an option for districts to dedicate a portion of their 1997-98 operational funds for facilities needs.
- An additional $59.4 million to implement a standardized testing program for all California students in grades 2 through 11.
- An additional $277.7 million (all funds) is provided for state child care programs to further augment the Governor's proposal to reform California's welfare system.
- The transfer of $100 million of property tax revenue to cities, counties, and special districts, as well as an additional $75 million to certain counties under the Disproportionate Share Hospital Program and $50 million to capitalize the California Infrastructure Bank.

The May Revision reflects a balanced budget, with General Fund expenditures held at $268 million below General Fund revenues. The May Revision also provides for a budget reserve of $580 million for economic uncertainties.

WHAT'S HAPPENED SINCE JANUARY

The following developments at the state and federal level have occurred since the Governor's Budget was submitted to the Legislature in January, and are reflected in the May Revision. A more detailed discussion of these issues can be found further in this document.

In the Economy. California's economic performance continues to outpace the nation in both personal income growth and job growth. The state's employment forecast for the next two years has been increased by 100,000 over the January budget, for a total of 680,000 new jobs.

In Revenues. General Fund revenues are now expected to be more than $960 million higher than anticipated for 1996-97 compared to the January forecast, and $1.3 billion higher in 1997-98 for a combined increase of $2.26 billion. The most important factor influencing the forecast has been substantial increases in personal income tax revenue, which accounts for $2.16 billion of the revenue change over the two years.

In Caseload Programs. Each of the state's principal entitlement programs—Medi-Cal, SSI/SSP, and AFDC/TANF—have been revised downward for both the current and the budget years. Prisoner and ward population estimates for the Department of Corrections and the Youth Authority, while continuing to increase on a year-over-year basis, are growing at slower rates than was forecast in January.

In Federal Issues. The May Revision assumes that the final federal budget agreement will restore Supplemental Security Income benefits to legal immigrants. Consequently, the proportionate state funding is restored in both the State Supplemental Payment and In-Home Supportive Services Programs. In the event that Washington fails to provide funds to the state for mandated illegal immigrant health care, the May Revision makes state General Fund available if part or all of the federal appropriation fails to materialize.

THE ECONOMY

THE NATION

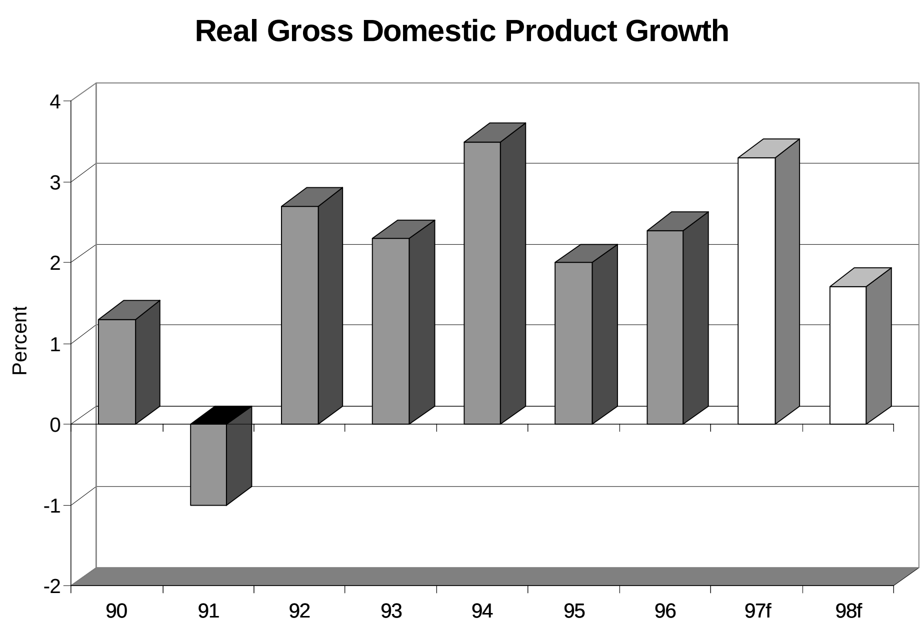
The U.S. economy strengthened markedly in late 1996 and early 1997. Real gross domestic product (GDP) grew at a robust 3.8-percent annual rate in last year's fourth quarter, and then surged at a 5.6-percent pace in the opening months of 1997, based on initial estimates. This first-quarter growth was the strongest in nearly a decade. Reinforcing the GDP figures, April's unemployment rate was estimated at 4.9 percent of the labor force, the lowest in 24 years.

The economy's resurgence was in sharp contrast to last fall's widely held expectations—on the part of most private analysts as well as Federal Reserve policy makers—of an impending slowdown in the nation's economy. The central bank would prefer to hold growth at or below a 2½-percent rate, which they judge to be the nation's long-run potential. There is concern that sustained growth above that pace risks the return of inflation.

At present, however, there are few if any signs of inflation. Prices paid in the U.S. (the deflator for gross domestic purchases) advanced at a modest 2.2-percent annual pace in the first quarter, down from a 2.6-percent rise in late 1996. Consumer prices increased at a 2.4-percent annual rate in the first three months of 1997. Total labor compensation costs, as measured by the employment cost index, rose a scant 0.6 percent in the first quarter, also a 2.4-percent annual rate.

On the basis of experience to date, the May Revision forecast of 3.3 percent real GDP growth for 1997 is 0.9 percent higher than in the January forecast. The May Revision forecast of a 2.6-percent inflation rate for 1997, as measured by the Consumer Price Index (CPI), is 0.7 percent lower than the January forecast.

FIGURE ECON-1



Partly on the assumption that the Federal Reserve will eventually have its way, 1998 growth is reduced to 1.7 percent, which is 0.8 percentage point less than the January Budget forecast. CPI inflation next year is forecast at 2.9 percent, 0.7 percentage point below the January assumption. The May Revision forecast reflects a further half-percent increase in the interbank federal funds rate, to 6 percent by this summer; the January forecast contemplated a drop in the overnight funds rate to 5 percent by mid-1997, and remaining at that level throughout 1998.

To summarize the U.S. forecast:

- Real gross domestic product is expected to grow 3.3 percent this year, but slow to a 1.7-percent pace in 1998.

- Unemployment is expected to average a little over 5 percent this year, and rise modestly to 5 ½ percent in 1998.

- Inflation will remain low, with consumer prices rising 2.6 percent in 1997 and 2.9 percent in 1998.

- Interest rates will rise modestly. The overnight federal funds rate is expected to reach 6 percent this summer, with the possibility of a reduction in short-term rates by late 1998. Longer-term interest rates may rise about one-quarter percent from recent levels, and should also decline slightly in 1998.

- The dollar is expected to remain strong this year, but will settle back in 1998 as economic growth slows.

FIGURE ECON-2

Selected U.S. Economic Indicators, 1996-98

	1996	1997	1998
Real gross domestic product (GDP), (1992 dollar) (Percent change)	2.4	3.3	1.7
Personal consumption expenditures	2.5	3.6	2.2
Gross private domestic investment	4.6	8.3	2.7
Government purchases of goods and services	0.8	1.1	0.5
GDP deflator (1992=100) (Percent change)	2.0	2.1	2.2
GDP, (Current dollar) (Percent change)	4.4	5.4	3.9
Federal funds rate (Percent)	5.3	5.7	5.9
Personal income (Percent change)	5.5	5.8	4.7
Corporate profits before taxes (Percent change)	6.8	4.0	-1.5
Nonfarm wage and salary employment (Millions)	119.5	122.2	124.2
(Percent change)	2.0	2.2	1.6
Unemployment rate (Percent)	5.4	5.2	5.4
Housing starts (Thousands)	1,466.8	1,445.0	1,332.7
(Percent change)	7.9	-1.5	-7.8
New car sales (Millions)	8.5	8.4	8.0
(Percent change)	-2.2	-1.3	-4.7
Consumer price index (1982-84=100)	157.0	161.1	165.7
(Percent change)	2.9	2.6	2.9

Forecast based on data available as of April 24, 1997. Percent changes calculated from unrounded data.

CALIFORNIA

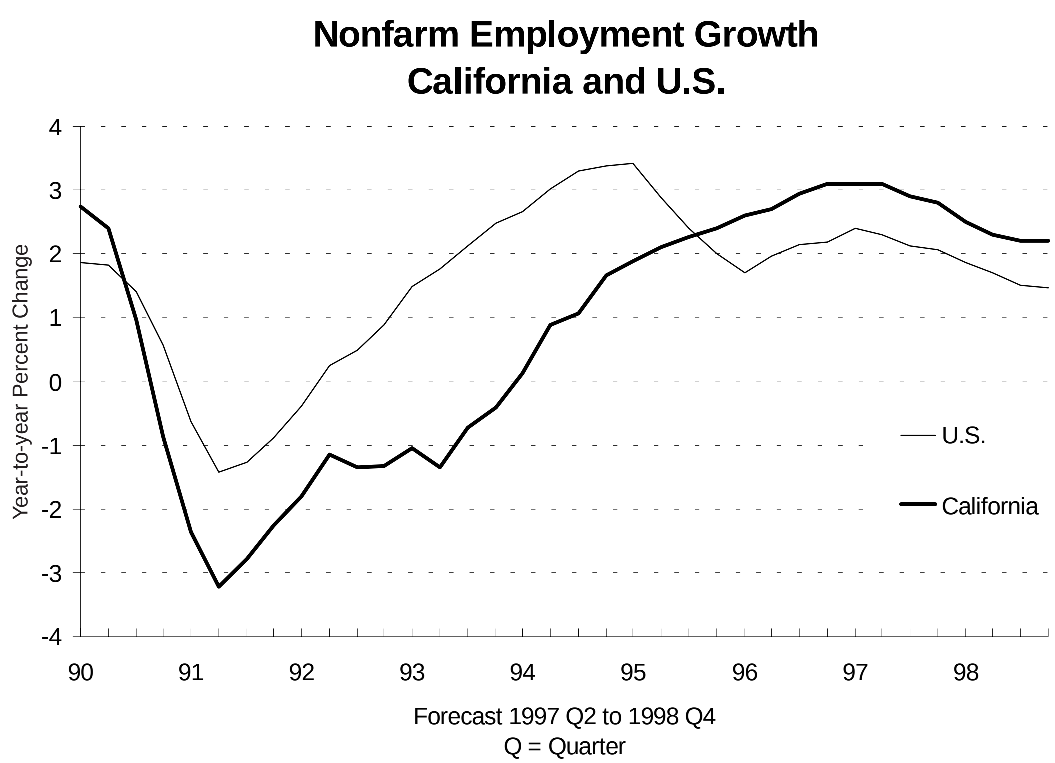
California's economy is continuing to experience strong, sustained growth. Nonfarm wage and salary employment increased at an annual rate of 400,000 jobs in this year's first quarter. The March 1997 unemployment rate of 6.5 percent was a full percentage point lower than a year ago.

The more vigorous national economy and strong first-quarter California job growth has resulted in an upward revision to the California forecast. This year, the state is on course to add 380,000 new jobs, 50,000 more than in the January Budget. In 1998, California is expected to create an additional 300,000 jobs, up from 250,000 in the January forecast (see Figure ECON-3). Thus, employment growth for the next two years has been increased by 100,000 over the January Budget, to a gain of 680,000 new jobs.

The revised 1997 unemployment rate of 6.3 percent is a half-percent lower than the January forecast, and the revised 1998 rate of 5.8 percent is nearly a full percentage point lower than was forecast in January. Personal income growth is revised up by 0.2 percentage point in both 1997 and 1998, a rate that continues to outpace the nation's growth rate. (See Figure ECON-4)

The State is benefiting from a unique industry mix that includes a wide array of high-technology manufacturing and service sectors, including electronic components, computers, instruments, software, motion pictures, multimedia and biotechnology. Growth in these industries has more than offset losses resulting from severe cuts in the nation's defense budget, which contributed to a 67-percent drop in aerospace employment between 1988 and 1995.

FIGURE ECON-3



THE ECONOMY

From the recession's low point in late 1993, California's economy has created more than one million new jobs through March 1997, and has eclipsed the previous May 1990 employment peak by nearly 300,000. The State's economy is marking another major milestone this year: gross state product is now exceeding the one trillion dollar level—the first time any state has achieved this magnitude of economic output.

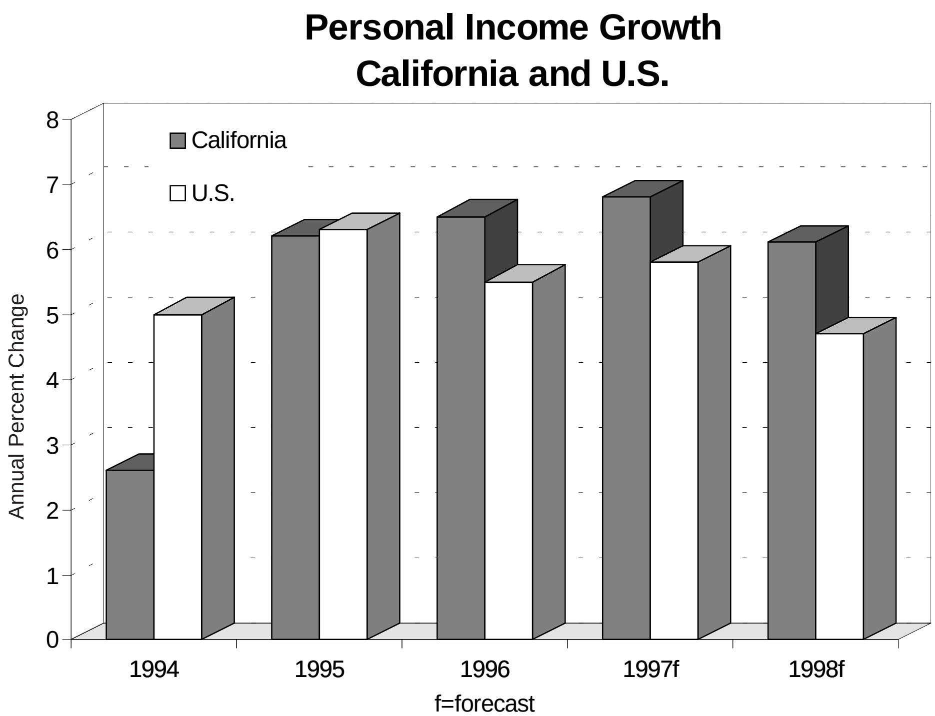
Many of the new high-growth industries are also high-wage industries. Wages in computer manufacturing average more than $64,000 per year; in software and multimedia industries, more than $68,000; in biotechnology, more than $60,000; and in motion picture production, more than $65,000. Growth in these high-wage jobs resulted in total wages increasing by more than double the rise in total employment in 1996.

Employment in manufacturing increased by 3.3 percent in 1996—a gain of almost 60,000 jobs. This represents the best job gain since 1984 and is in sharp contrast to a loss of nearly 250,000 factory jobs in the other 49 states. The long decline in aerospace appears to have bottomed out—the industry added 1,400 jobs over the past year reflecting a pickup in the commercial segment of the business.

International trade also contributes to the State's economic growth. In spite of a stronger dollar and sluggish economic performance by many industrial trading partners, foreign trade through California ports continued to expand in 1996—with total trade volume of just under $300 billion. Exports shipped via California ports grew by 6.3 percent and imports rose by 2.9 percent over 1995. Importantly, exports of California-made goods—shipped from California and elsewhere—rose more than 8 percent in 1997, nearly double the growth of exports nationwide.

California inflation has been revised down 0.4 percentage point compared to the January forecast. This is less than the revision to national inflation and is due to housing cost pressures in the Bay Area.

FIGURE ECON-4



Highlights of the California forecast include:

- ◆ Employment is projected to grow faster than the nation for the next two years, with an increase of 3 percent in 1997 and 2.3 percent in 1998—680,000 new jobs over the next two years. Unemployment is expected to drop to 6 percent by the end of 1997.
- ◆ Personal income growth is expected to remain strong—increasing by 6.8 percent in 1997 and 6.1 percent in 1998.
- ◆ Inflation will remain below the national average. Consumer prices in California are expected to increase by 2.3 percent in 1997 and 1998. Real purchasing power, therefore, will rise by an average of more than 4 percent per year over the next two years.
- ◆ Homebuilding is forecast to increase moderately to 110,000 units this year and 122,000 in 1998. Stronger job-generated demand is being offset by a forecast of higher interest rates. In response to low office and industrial vacancy rates, nonresidential construction is expected to show strong growth—with last year's double-digit growth continuing in 1997 and 1998.

FIGURE ECON-5

Selected California Economic Indicators

			Forecast			
	1996	Percent Change	1997	Percent Change	1998	Percent Change
Personal income (dollars in billions)	810.1	6.5%	865.2	6.8%	917.7	6.1%
Nonfarm W&S employment (thousands)	12,775	2.8%	13,154	3.0%	13,450	2.3%
Mining	30	-1.5%	29	-0.3%	29	-1.2%
Construction	511	5.2%	553	8.2%	584	5.6%
Manufacturing	1,853	3.3%	1,900	2.5%	1,940	2.1%
High Technology	498	4.1%	516	3.5%	529	2.7%
Transportation/utilities	641	1.8%	651	1.5%	654	0.4%
Whlse & retail trade	2,973	2.0%	3,045	2.4%	3,097	1.7%
Finance group	733	0.2%	730	-0.4%	732	0.2%
Services	3,917	5.0%	4,117	5.1%	4,277	3.9%
Government	2,117	0.5%	2,128	0.6%	2,138	0.5%
Unemployment rate	7.2%	--	6.3%	--	5.8%	--
Housing permits (thous.)	94	8.9%	110	17.6%	122	10.7%
Consumer price index	157.1	2.0%	160.7	2.3%	164.5	2.3%

Forecast based on data available as of April 24, 1997. Percent changes calculated from unrounded data.

REVENUE ESTIMATES

Revenues are projected to be above the 1997-98 Governor's Budget forecast by $960 million in 1996-97 and $1.303 billion in 1997-98, for a combined increase of $2.263 billion. These increases are a reflection of recent cash experience, as well as recalibration of the tax models that incorporate the 1995 personal income sample data and the revised economic data. Based upon the May projections, revenues are expected to grow 6.6 percent between 1995-96 and 1996-97. From 1996-97 to 1997-98, revenue growth is estimated at 5.3 percent, which is lowered somewhat due to the Governor's tax reduction and trial court funding proposals.

The May Revision reflects the Governor's tax reduction initiatives, including a 10-percent bank and corporation tax reduction phased in over two years, full conformity with recent federal changes relating to Subchapter S corporations, and conformity with increased federal limits on small business expensing. In addition, consistent with the Governor's Budget, the estimate assumes that legislation will be adopted at the federal level providing California with the authority to establish a reciprocal refund offset program with the Internal Revenue Service for past-due state tax debts.

PERSONAL INCOME TAX

Extremely strong growth in personal income tax revenues accounts for most of the change in the revenue forecast. Actual tax return data for the 1995 tax year and cash receipts for 1996 indicate that taxpayers have realized significant income gains that have pushed them into higher marginal tax brackets. This has resulted in revenue growth far in excess of income growth. Wage growth during 1995 and 1996 was 5.1 percent and 6 percent, respectively, while the growth in personal income tax liability increased 12.4 percent and 14 percent, respectively. This 14-percent growth in 1996 is even more impressive given the fact that the 10 and 11 percent tax brackets had expired. On a comparable basis, growth for the year would be closer to 19 percent.

A surging stock market contributed heavily to the 22-percent increase in capital gains in 1995 and is undoubtedly an important factor in the 1996 tax year growth. Partnership and Subchapter S shareholder profits also exhibited unusually strong gains over the last two years. In part, this reflects the decisions of increasing numbers of corporations to choose the Subchapter S form of organization, where the entity pays a reduced tax rate and the income and losses flow through to shareholders. These increases are probably also a reflection of healthy profit growth. Bonus and stock option activity also boosted wage growth, particularly at higher income levels. Based on recent cash experience, these trends appear to be continuing and were therefore built into the revenue forecast through the budget year.

SALES TAX

Sales and use tax revenues have been tracking the Budget forecast closely. The May Revision forecast was revised downward by $55 million in 1996-97 and $95 million in 1997-98 to reflect recent cash experience and the most recent economic forecast. Although taxable sales during the first half of the 1996 calendar year were exceptionally strong, increasing 7.8 percent from the prior year, the third and fourth quarters for the year posted a more moderate gain of 5.8 percent. On a fiscal year basis, revenues are anticipated to be up by 4.3 percent for 1996-97 and 4.9 percent for 1997-98, reflecting steady economic growth throughout the forecast period.

BANK AND CORPORATION TAX

Bank and corporation tax revenues have been very close to the forecast and therefore were revised only slightly. The forecast has been reduced by $25 million in 1996-97, primarily due to revised net accrual estimates. In 1997-98, revenues are expected to be higher than anticipated in January by $60 million, reflecting a somewhat healthier economic outlook. The weakness that was apparent in the year-end prepayments last year seems to have been due to one-time adjustments by corporations and current payment levels are showing encouraging gains. Therefore, the May Revision estimate reflects continued moderate profit growth through the forecast period.

OTHER REVENUES

Higher insurance tax collections account for $66 million of the forecast increase in 1996-97 and $17 million in 1997-98. This gain reflects higher premium growth rates than were anticipated in January. Strong stock market gains and economic growth have also resulted in increased estate tax revenues. This forecast anticipates estate tax revenues will be up $22 million in 1996-97 and $40 million in 1997-98. As with the Governor's Budget forecast, this estimate assumes that the Governor's proposal to restructure trial court funding will be enacted. This shifts revenues out of the General Fund in 1997-98.

FIGURE REV-1

General Fund Revenue Forecast
Reconciliation with the Governor's Budget Forecast
(Dollars in Millions)

Source	Governor's Budget*	May Revision	Change Between Forecasts	
Fiscal Year 1995-96				
Personal Income Tax	$20,875	$20,875	$0	0.0%
Sales & Use Tax	15,753	15,753	0	0.0%
Bank & Corporation Tax	5,862	5,862	0	0.0%
Insurance Tax	1,132	1,132	0	0.0%
Other Revenues	2,413	2,413	0	0.0%
Transfers	261	261	0	0.0%
Total	**$46,296**	**$46,296**	**$0**	**0.0%**
Fiscal Year 1996-97				
Personal Income Tax	$22,660	$23,560	$900	4.0%
Sales & Use Tax	16,485	16,430	-55	-0.3%
Bank & Corporation Tax	5,795	5,770	-25	-0.4%
Insurance Tax	1,124	1,190	66	5.9%
Other Revenues	2,273	2,349	76	3.3%
Transfers	68	66	-2	-2.9%
Total	**$48,405**	**$49,365**	**$960**	**2.0%**
Change from Fiscal 95-96	$2,109	$3,069		
Percent Change from Fiscal 95-96	4.6%	6.6%		
Fiscal Year 97-98				
Personal Income Tax	$24,240	$25,500	$1,260	5.2%
Sales & Use Tax	17,325	17,230	-95	-0.5%
Bank & Corporation Tax	5,860	5,920	60	1.0%
Insurance Tax	1,196	1,213	17	1.4%
Other Revenues	1,943	2,004	61	3.1%
Transfers	93	93	0	0.0%
Total	**$50,657**	**$51,960**	**$1,303**	**2.6%**
Change from Fiscal 96-97	$2,252	$2,595		
Percent Change from Fiscal 96-97	4.7%	5.3%		

*The Governor's Budget forecast has not been adjusted for the Governor's April proposals for full Subchapter S conformity and small business expensing which reduce the 1997-98 forecast by $40 million.

EDUCATION

PROPOSITION 98 GUARANTEE

1996-97 $885.8 million
1997-98 $1,213.3 million

When the Governor's Budget was presented in January, Proposition 98 appropriations were estimated to increase above the 1996 Budget Act level by $261.6 million in 1995-96 and $341.8 million in 1996-97, and K-12 dollars per pupil were estimated to grow a total of $374 between 1995-96 and 1997-98, from $4,636 to $5,010. The May Revision reflects significant increases in estimated state revenues and K-12 average daily attendance (ADA), and a substantial revision to the estimated state civilian population. In addition, the May Revision includes a moderate revision to the local property tax growth estimates (from 1.5 percent to 1.2 percent in 1996-97, and from 3.5 percent to 3.0 percent in 1997-98) and a $100 million transfer of property taxes from the Educational Revenue Augmentation Fund (ERAF) back to local taxing agencies. The effect of these revised estimates combine to increase the State's share of the Proposition 98 guarantee by a total of $2.2 billion, $111.3 million in 1995-96, $885.8 million in 1996-97, and $1,213.3 million in 1997-98. The revised K-12 dollars per pupil increased another $141 above the January estimate, jumping to $5,151 in 1997-98, an increase of 10.6 percent above the $4,656 in 1995-96 (see Figure K12-2).

FIGURE K12-1

PROPOSITION 98
January vs. May Revision
(Dollars in Thousands)

1996-97	January Proposal	May Revision	Change
General Fund	$19,419,699	$20,305,481	$885,782
Local Revenue	10,096,406	10,067,815	-28,591
Total Guarantee	$29,516,105	$30,373,296	$857,191

1997-98	January Proposal	May Revision	Change
General Fund	$20,985,539	$22,198,856	$1,213,317
Local Revenue	10,443,311	10,269,884	-173,427
Total Guarantee	$31,428,850	$32,468,740	$1,039,890

Appropriations counting toward the 1997-98 guarantee continue to include a $200 million loan repayment pursuant to Chapter 78, Statutes of 1996.

EXPENDITURES

K-12 EDUCATION

1996-97 $793 million
1997-98 $1,106 million

The May Revision dedicates nearly 90 percent of all new General Fund revenues to K-12 education, the Administration's highest priority. This increase provides more than $2 billion in additional resources above the January budget. From the time the 1995-96 Budget Act was signed by the Governor, an additional $5.3 billion from the State General Fund has been added to the Proposition 98 K-12 budget. The additional General Fund for Proposition 98 in 1996-97 and 1997-98 is $3.6 billion just since the 1996 Budget Act was signed (see Figure K12-3). Total General Fund allocations of $21.9 billion for K-12 education now represents 42.3 percent of the total General Fund budget.

The May Revision includes estimated K-12 ADA growth for 1996-97 of 3.34 percent, up from 2.45 percent in the Governor's Budget. This results in an ongoing increase of $256 million. In the budget year, the revised ADA growth rate is reduced slightly, from 2.35 percent in January to 2.06 percent. After adjusting for the current year increase, there is a net budget year increase of $182.5 million.

A substantial portion of the new Proposition 98 funds will be spent for school district equalization and deficit reduction, pursuant to legislation enacted along with the 1996 Budget Act. In addition to equalization and deficit reduction, the increase in K-12 funds allows the Governor to continue pursuing significant new programs which will assist the schools to improve the quality of education for California's 5.6 million K-12 pupils.

CURRENT YEAR

School district and county office of education revenue limit continuous appropriations increase by $190.9 million since the Governor's Budget, resulting from increased estimates of ADA and a small decrease in local property tax revenues.

While the Governor's Budget projected increased ongoing funding of $304.2 million for school district equalization and deficit reduction starting in 1996-97, pursuant to Chapter 203, Statutes of 1996, the May Revision includes a further increase of $383.7 million in ongoing equalization and deficit reduction, for a total ongoing level of $687.9 million. The May Revision also includes one-time funding of almost $345 million including the following:

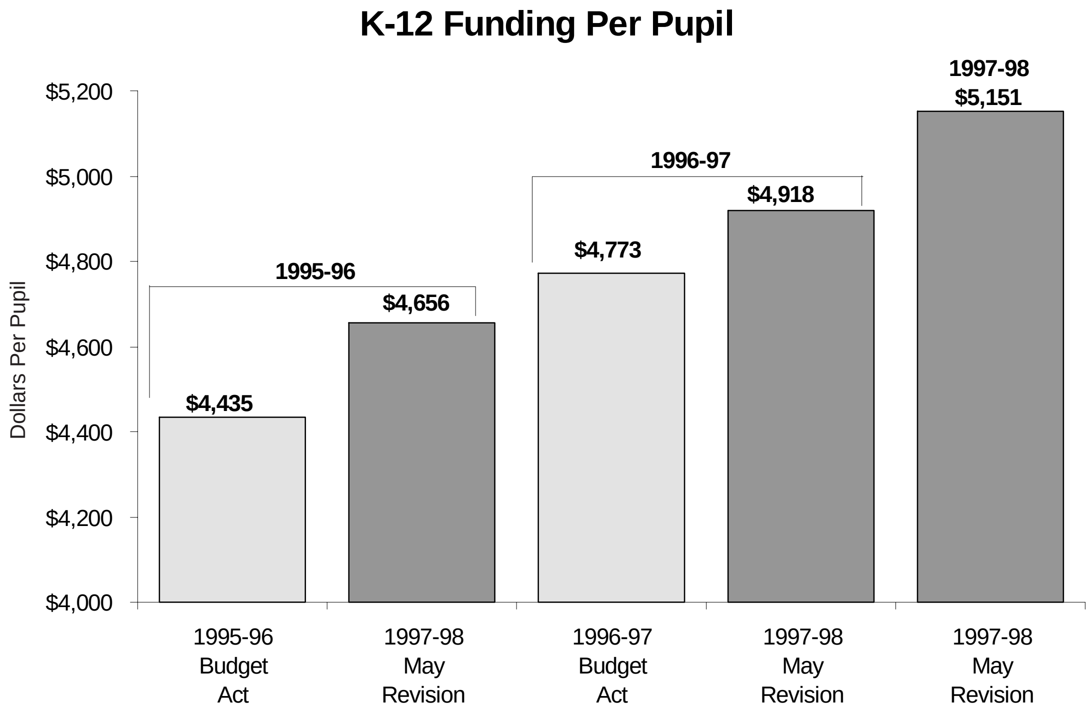
▲ $150 million appropriated as a reserve for payment of claims received from school districts and community college districts for the reimbursement of state-mandated local costs for 1994-95 through 1996-97.

▲ $100 million in 1995-96 settle-up for K-12 Deferred Maintenance; when matched with existing appropriations and local match, this will provide $270 million in 1997-98.

▲ $59.5 million to fund the current-year deficiency in Special Education program entitlements, based upon actual data now available for 1995-96, in addition to upward K-12 ADA growth.

▲ $20 million augmentation to the $15 million proposed in the Governor's Budget for the purchase of new child care facilities. This program will increase the availability of portable classrooms to approximately 370 in order to replace classrooms displaced for class size reduction and to accommodate recent and proposed expansions of subsidized, center-based child care.

FIGURE K12-2



▲ $8 million augmentation in 1995-96 settle-up funds to the Standard Account Code Structure, increasing total funding provided for this program to $17 million.

Equalization/Deficit Reduction. The May Revision includes a total of $1.4 billion, $688 million in the current year and $722 million in the budget year, to be applied toward school district equalization and deficit reduction. Chapter 203, Statutes of 1996, specifies that any additional funds available for appropriation in the 1996-97 fiscal year be allocated on a 50-50 basis for school district equalization and deficit reduction. This amount is calculated after giving community colleges their share of the increase, and after making adjustments for ADA growth and other deficiencies.

In January, the amount provided for equalization and deficit reduction was estimated to be a total of $616 million for the current and budget year. Because these new funds, which now total $1.4 billion, represent such a significant portion of the additional general purpose money available to schools, the Governor is requesting that school districts consider carefully how these funds will be spent. In proposed language, school districts will be required to discuss expenditure plans at a public hearing of the local governing board, and to submit a report to the State, detailing their expenditure plans. This will ensure that the public, the Administration, and the Legislature are aware of local priorities for this new infusion of dollars.

The May Revision also recognizes several deficiencies which occurred in the current year, which are applied toward the 1996-97 Proposition 98 guarantee prior to the equalization/deficit reduction calculation.

Reserve for Mandates. The May Revision includes a $150 million appropriation as a reserve for payment of claims received from school districts for the reimbursement of state-mandated local costs for 1994-95 through 1996-97. Actual payments to any district will not be made until its claims have been audited.

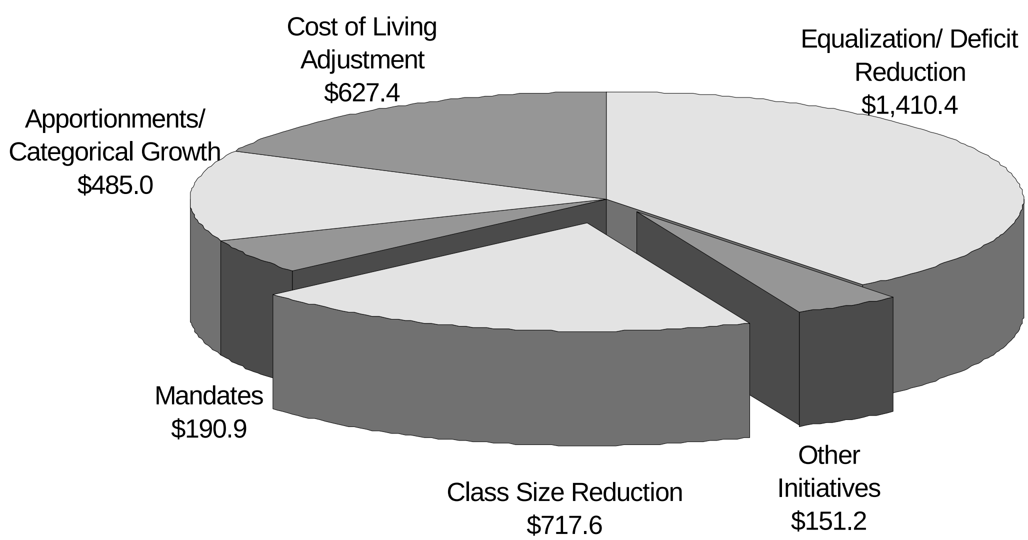
BUDGET YEAR

For 1997-98, State General Fund support of K-12 education will increase by $1.1 billion which results from changes in property tax growth ($147.0 million), ADA ($182.5 million) and the combined effect on the Proposition 98 guarantee of revising estimates of state revenues and population ($776.1 million). With this increase, the total increase from the current year to the budget year in State General Fund for K-12 education is now projected to be $1.7 billion. The May Revision includes the following significant changes for 1997-98:

- ▲ $229.6 million to increase the incentive payments for the Class Size Reduction Program.
- ▲ Increasing districts' ability to expand implementation of Class Size Reduction by allowing districts to apply one-time savings for facilities grants of $40,000 for each new class needed. No additional funding is necessary for this proposal.
- ▲ $277 million augmentation of Proposition 98 ($64 million) and Federal Funds ($213 million) for additional expansion of direct child care services to meet the rising demand for child care services for both low-income families and those families who are moving from welfare to work.
- ▲ $82.6 million, including a $59.4 million augmentation and a $23.2 million redirection, to provide a standardized program for individual pupil assessments.

FIGURE K12-3

Proposition 98 General Fund
K-12 Expenditures
What the $3.6 Billion Two-Year Increase Buys
(Dollars in Millions)



EXPENDITURES

▲ $50 million to double the funds for the first year of the Governor's Digital High School initiative which will provide funds for grants to approximately 200 high schools for major educational technology installations.

▲ $57.1 million to augment the block grant for programs in the categorical Mega-Item, for allocation on the basis of an equal amount per ADA to be used locally to support any program in the Mega-Item as well as deferred maintenance.

▲ $28.1 million increase in school district, county office of education, and special education apportionments to reflect an increase in cost-of-living adjustment from 2.53 percent to 2.65 percent.

▲ $11.3 million for Adult Education program growth and $13.3 million for Regional Occupational Center and Program Growth.

▲ $18.9 million reduction to the General Fund needed for the Special Education Program resulting from a combination of changes. (See *Special Education Program* for details.)

Class Size Reduction Program. In 1996-97, $771 million was appropriated as incentive funding for the Class Size Reduction (CSR) Program to encourage districts to reduce class sizes in three grades by reducing grades one and two and either Kindergarten or grade three. School districts receive $650 per pupil for any class which does not exceed a 20:1 pupil/teacher ratio for the entire day, and $325 per pupil for a pupil/teacher ratio which does not exceed a 20:1 for half the school day. The 1997-98 Governor's Budget proposed to augment the CSR Program by $488 million to increase the incentive rates by a cost-of-living adjustment, and to add an additional grade. Recent surveys by the Office of Child Development and Education (OCDE), the Department of Finance, the Legislative Analyst's Office, and education organizations have provided evidence to support changes needed to the CSR Program to provide more funding and, in limited circumstances, more program flexibility. These surveys have shown that the most suitable funding level for CSR is $800 for the full-day option and $400 for the half-day option. The May Revision includes an augmentation of $229.6 million to fund these higher rates.

In addition to the rate increase, the Administration will propose language to increase program flexibility to provide districts with options to customize the implementation of CSR to their own unique situations, so that certain family hardships would be avoided and disruptions in the educational settings for Limited English Proficient (LEP) students would be mitigated. In addition, the Administration proposes to allow CSR classes being implemented in the budget year, above the current year base number of classes, to start in February 1998, and receive full-year funding. Teachers for these classes would be required to be hired by November 1, 1997, and provided with all required staff development before assuming responsibility for their own classes.

Class Size Reduction Facilities Grants. Although the Budget sets aside funds for operations grants for statewide K-3 implementation, not every district will be able to fully implement CSR in four grades because there will not be sufficient classroom space. The Administration proposes allowing districts flexibility by using a portion of the operational stipend funds to acquire more classroom space to meet the facilities' needs for 1997-98 expansion of CSR. For 1997-98, districts may receive a "loan" of $40,000 for new classrooms needed for further expansion of CSR in 1997-98, pursuant to the existing eligibility criteria in the CSR Facilities Funding Program. The maximum total of such loans would be limited to one-half the amount of operational stipend needed to complete full implementation of the CSR Program. If a district certifies at the end of the year that they actually expanded CSR to the number of new classes for which a loan was received, the loan would be forgiven. This is an interim proposal that provides facilities funding until a bond can be placed before the voters.

Child Care Growth and Expansion Program. The adequate provision of child care is a critical component of the Governor's proposed welfare reform plan. It is also critical to many families struggling to raise families without welfare assistance. The May Revision addresses both of these areas by providing an additional $277 million in direct services. Coupled with the $107 million of additional local assistance funding already proposed in the Governor's Budget, the total proposed augmentation reflects a significant and balanced commitment to the needs of the State's low-income populations and represents approximately a 42 percent increase in expenditures for the State's subsidized child care programs. This additional commitment in the May Revision includes a proposed transfer of $213 million from the Temporary Assistance for Needy Families (TANF) block grant to the Child Care and Development block grant to fully address the TANF-related child care needs. These services will be accomplished through an increase in interagency transfers to the Department of Social Services for distribution to counties.

Additionally, a $64 million increase of Proposition 98 funds is proposed for State Department of Education-administered child care programs. This component includes a $45 million augmentation to General Child Care for expansion of services for infants and children under three years of age. Current access to high-quality licensed child care for mothers who work and have very young children is limited. As more low-income mothers with children under three enter the workforce, these additional funds will help ensure the availability of licensed, developmentally appropriate child care which is critical at the early stages of a child's life. In addition, a $15 million augmentation is proposed to the State Preschool Program which provides a quality developmental experience for three and four year olds to better prepare them for school. Allowing for lead time to develop provider capacity, these two augmentations reflect half-year funding and a $120 million commitment on an annual basis to provide services to approximately 25,000 more infants and children under kindergarten age. Finally, the May Revision proposes an additional $4 million to augment the School Age Parenting and Infant Development Program to provide services to an additional 1,500 school-aged parents and their children while the parents finish school.

Adult Education Program. As part of the State's overall welfare reform effort, the Administration proposes to target $50 million of the funds available for the Adult Education Program to provide educational services specifically to TANF recipients. Educational services to be funded from the targeted $50 million will include those designed to increase self-sufficiency, job training, and work. The existing Adult Education Program offers a number of classes, including those in adult basic education, short-term vocational training, parenting education, and English-as-a-Second Language (ESL), that can provide necessary skills to TANF recipients making the transition from welfare dependency to self-sufficiency and work.

Local Assessments Program. The Governor's Budget included $23.2 million to support the local incentive testing program established as part of the California Assessment of Academic Achievement Program enacted by Chapter 975, Statutes of 1995 (SB 265). This program provides incentive funding of $5 per pupil tested to all districts that administer locally-adopted tests to all pupils in grades 2 through 10. These tests are to focus on basic academic skills and provide valid, reliable, and comparable individual student scores to parents and teachers. The May Revision includes an augmentation of $59.4 million to implement a required testing program for all pupils in grades 2 through 11. With the $23.2 million redirected from the current incentive program, the total available for this new assessment program will be $82.6 million. All students will take the same exam for a particular grade level or subject and statewide comparability of scoring will be achieved. All exams would be selected by the State Board of Education from among those developed by publishing companies. As in the current program, individual results will be reported to students and parents.

Digital High School Program. Computer knowledge and skills are necessary for both individual success and statewide prosperity. Because high school students are the closest to entering the job market, beginning a major technology initiative at the high school level is the most effective approach. Through broadly defined matching requirements and waiver flexibility, this program assures that all high schools can become Digital High Schools and achieve a high level of technology integration throughout their curriculums. This well-balanced approach to technology includes provisions for ongoing technical support, system upgrades, and staff development. In January, the Governor proposed $50 million to begin this four-year initiative. The May Revision provides an additional $50 million to double the number of first-year grants. This will provide grants to approximately one-quarter of the State's high schools, bringing the level of funding in line with the goal of providing grants to all high schools within four years.

Goals 2000 Program. California's share of Goals 2000 funding available in 1997-98 from two years of federal funding increments is estimated to be $93.9 million. The Governor's Budget included an expenditure plan for these funds. Since that time, the Administration has been working closely with the California Department of Education to refine the plan so it best addresses the priorities of both the Administration and the California Department of Education. As a result of these efforts, the May Revision revises the expenditure plan for Goals 2000 funds. Funds will be deleted or reduced to:

- eliminate $1.4 million for support of the Standards Commission and shift these costs to the General Fund,
- reduce funding for the donated computers program from $10 million to $6 million and fund the remaining $4 million from the General Fund,
- eliminate the $2 million for staff development for math instruction, and
- reduce the amount for reading handbooks for teachers from $500,000 to $200,000 to reflect revised cost estimates.

Funds will be added or increased to:

- use $1.8 million to fund competitive programs in support of libraries and the arts,
- use $4 million to support a computer technology program sponsored by the Superintendent of Public Instruction,
- use $1 million to replace a non-Proposition 98 General Fund augmentation proposed in the Governor's Budget for the Advancement Via Individual Determination (AVID) Program which encourages students to seek post-secondary education, and
- increase the amount to California Department of Education for grant administration from $500,000 to $1.4 million.

Special Education Program. State General Fund support for the Special Education programs will decrease by $18.9 million in the budget year due to a combination of changes. These changes include an estimated increase of $23.1 million in entitlements attributable to funding the current-year deficiency in growth and an increase in state support of $1.4 million due to a decrease in federal funds available for local agency entitlements. Offsetting these increases in state support are a decrease of $9.1 million in the amount needed for growth, a decrease of $30.2 million due to increased revenue limit funding available for Special Day Classes, and a decrease of $4.1 million to reflect excess ERAF collections.

CALIFORNIA COMMUNITY COLLEGES

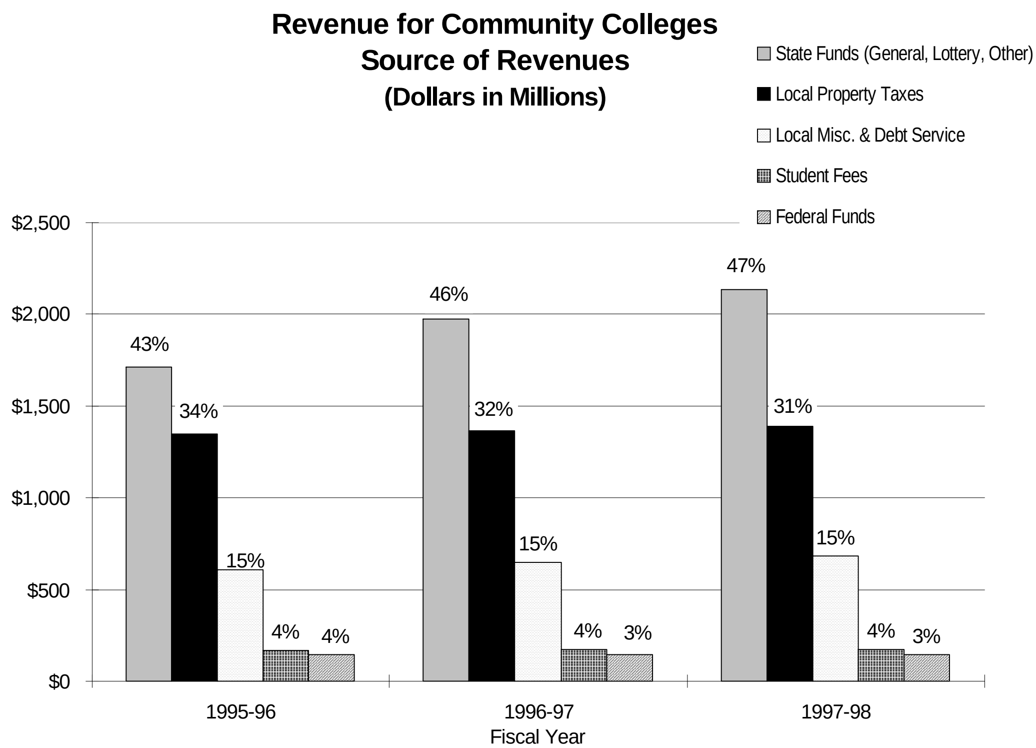
1996-97 $93.0 million
1997-98 $108.1 million

CURRENT YEAR

For 1996-97, the Governor's Budget included $59.4 million in one-time funds proposed through legislation to satisfy the revised minimum Proposition 98 guarantee for prior years. The May Revision includes an additional $93 million in one-time funds from the 1996-97 guarantee. This is proposed to fund the following significant changes:

- ▲ $65.2 million to augment the full-time equivalent student-based block grant for a total of $118.7 million, which may be used for high-priority instructional equipment, technology infrastructure, library material replacement, and scheduled maintenance and special repairs. This provides about $1.1 million to an average-sized community college.
- ▲ $20 million to augment the scheduled maintenance and special repair match program.
- ▲ $4 million to augment the funding for child care facilities to support expanded services to welfare recipient students. This brings the total for community college child care facilities to $10 million.
- ▲ $2 million to backfill a property tax deficit pursuant to the final calculation of excess taxes for 1995-96.

FIGURE HIED-1



BUDGET YEAR

Overall revenues for Community Colleges are estimated at $4.5 billion from all fund sources in 1997-98, a $232.7 million increase over the estimate for 1996-97 (5.4 percent). Absent one-time funding increases from the current year guarantee totaling $127.8 million, ongoing expenditure growth included in the Budget is 8.6 percent.

For 1997-98, the May Revision includes a net increase of $108.6 million over the Governor's Budget proposal, including the following significant ongoing changes:

- ▲ $24.3 million to increase the amount of growth funds ($18.3 million) to provide a three-percent increase in the number of students, and to increase the COLA ($6.0 million) to reflect the change in the index to 2.97 percent for both general apportionments and categorical programs.

- ▲ $28.8 million to increase ongoing allocations for replacement of instructional equipment and library materials for high-priority needs.

- ▲ $15 million to increase the economic development program to fund cooperative industry-driven instructional and training programs, focused on the key industries in California's regional economies.

- ▲ $10 million to increase services to welfare-recipient students to address the work training requirements of welfare reform.

- ▲ $5 million to fund faculty and staff development in the use of technology to enhance learning, access, and student success through an increase to the telecommunications and technology infrastructure program.

- ▲ $26.4 million increase to reflect the revised estimate of property taxes.

Additional Growth. To meet critical needs of the community college system and increase access for California students, an additional $18.3 million is proposed for growth for general apportionments and categorical programs. This additional growth money, when combined with the general growth money proposed in the Governor's Budget, is estimated to fund an additional 27,500 full time equivalent students. This is proposed in recognition of need for a skilled workforce in an expanding economy.

Economic Development Program. The $15 million proposal for this program adds a new component to partner districts with key regional industries to fund curriculum design, instructional cost, and equipment to encourage expansion of industry-driven, cooperative education and workforce training programs which support California's regional economies.

The existing $9 million Economic Development Program provides small grants to develop instructional programs targeted to small businesses and emerging technologies. However, no state funding is currently targeted for the cost of instruction for industry-specific skills, nor to assist with equipment and other program startup costs. Through targeted growth and matching funds, this program will attract and leverage more industry involvement and, thus, encourage replication of successful models to other regions and industries, such as that exhibited in Santa Monica College's Academy for Entertainment and Technology.

Special Services for TANF Recipients. This proposal is to add $5 million for a curriculum redesign component and an additional $5 million to the child care component of the $53 million new program initiated in the Governor's Budget bringing the total to $63 million. The new component will allow districts to repackage or develop new curriculums to better integrate basic skills with vocational instruction and shift to a more intensive, open entry/open exit format as requested by counties and the Department of Social Services in conjunction with the current Greater Avenues For Independence (GAIN) Program. This is necessary to ensure compliance with the training limitations of California Temporary Assistance Program (Cal-TAP). Also, since child care is a critical component to successful training and transition to self-sufficiency, the Administration has re-evaluated the level of funding in the initial proposal for this component. With the proposed augmentation, a total of $15 million will be available for child care for TANF recipients.

HEALTH AND WELFARE

The 1997-98 May Revision includes $14.6 billion General Fund for Health and Welfare programs, up $8.8 million from the Governor's January Budget, and $23.0 million below the March/April Finance Letters. The Budget continues to assume that the State's welfare program will be redesigned effective January 1, 1998, prior year grant reductions will be made permanent, and automatic cost-of-living increases will be eliminated.

Caseload trends overall in the Health and Welfare area are generally lower than projected in January, including significant declines in Medi-Cal and the Aid to Families with Dependent Children (AFDC)/California Temporary Assistance Program (CalTAP).

The May Revision assumes that the final federal budget will restore Supplemental Security Income/ State Supplemental Payment (SSI/SSP) Program eligibility for legal immigrants. The May Revision also includes General Fund for the costs of health care services to illegal immigrants should federal funds not be made available for this purpose. Lastly, the May Revision proposes major expansions for the AFDC/CalTAP Program in the job training and child care program areas.

DEPARTMENT OF HEALTH SERVICES

MEDI-CAL

1996-97 -$59.3 million
1997-98 $155.0 million

CURRENT YEAR

The May 1997 Medi-Cal estimate projects total expenditures of $18.4 billion in the current year, including $6.8 billion General Fund for benefits and administrative costs. The May Revision reduces the deficiency estimate for 1996-97 by $43.2 million (-$59.3 million General Fund) to approximately $688.7 million total funds or about $373.4 million General Fund. A significant portion of this deficiency, $215.6 million, is due to the failure of the federal government to provide adequate funding for illegal immigrant health care costs. The remainder of the deficiency is Medi-Cal base expenditures.

The number of persons projected to be eligible for Medi-Cal in the current year is down from the January projection by 146,000 eligibles to 5,378,000. This represents a caseload decline of 2.7 percent from the January budget.

While caseload is down 2.7 percent, costs are down less than 1 percent since Medi-Cal expenditures are affected more by utilization of services. Much of the decline in caseload has occurred among AFDC-linked beneficiaries, women and children. This segment of the population uses fewer Medi-Cal services compared to the beneficiaries who are aged, disabled, and in long-term care facilities. The latter population needs a high level of medical services. For instance, beneficiaries residing in long-term care facilities represent only 1.3 percent of the Medi-Cal population but use almost 16 percent of total service costs.

Costs have also been tempered by lower-than-anticipated usage of a drug recently approved for treatment of AIDS patients.

The remaining changes reflected in the May Revision for Medi-Cal are relatively minor and include changes in drug rebates, county administrative costs, increased federal funding for minor consent eligibles, and federal delays in terminating services to persons who are disabled due to alcohol and substance abuse.

BUDGET YEAR

Total Medi-Cal expenditures for 1997-98 are estimated to be $19.1 billion. The General Fund amounts included in this total are $6.8 billion for traditional Medi-Cal local assistance expenditures and $34.6 million for capital debt. In addition, $215.6 million General Fund has been included for appropriation if the federal government does not appropriate funding for the cost of providing emergency medical care to illegal immigrants as authorized in federal law (HR 3610, Public Law 104-208).

The General Fund estimate has increased by $155 million to $7.1 billion. This change reflects the funding of illegal immigrant costs discussed above, reducing the state's administrative fee for the Disproportionate Share Hospital Program from approximately $230 million to $155 million ($75 million), long-term care increases ($23 million), and a reduction of drug rebate collections ($19 million). In addition, the May Revision includes a number of reductions due to caseload declines ($90 million), lower-than-anticipated use of a new AIDS drug ($54 million), reduced debt service payments for the hospital construction program as a result of project delays ($32 million) and elimination of eligibility processing for legal immigrants who will now remain on the SSI/SSP Program ($17 million).

The average monthly Medi-Cal caseload for 1997-98 is projected to be 5,268,000, which represents a reduction of 333,000 or 5.9 percent from the estimate reflected in the Governor's Budget. As mentioned in the current year narrative, however, the decline in Medi-Cal caseload does not correlate directly to declining costs due to varying levels of program use by different Medi-Cal beneficiary aid categories.

The Governor's Budget assumed the state-only program of prenatal care for illegal immigrant women would be terminated through regulatory changes expected to be approved by July 1, 1997. It now appears the regulations will be effective on that date. However, in order to provide appropriate notification to the counties and train eligibility workers on the new requirements, termination of eligibility for the existing caseload will be delayed until August 1, 1997. The May Revision, therefore, includes $7.1 million to provide services for one month.

As mentioned above, the May Revision includes a $75 million funding shift from the Medi-Cal Inpatient Adjustment Fund to the General Fund. The reduction in the administrative fee reduces the financial burden on publicly operated hospitals. This funding shift provides stability to this program which is an important source of indigent health care funding for California's "safety-net providers".

PUBLIC HEALTH

1996-97 - $5.2 million
1997-98 $5.8 million

CURRENT YEAR

AIDS Drug Assistance Program (ADAP)

The availability of more effective and expensive drugs and combination drug therapy from the ADAP formulary continues to increase demand and costs in this program. Maintaining drug treatment benefits for eligible HIV-infected persons will require an additional $5.8 million in the current year. Of this amount, $5.3 million is available from an increase in federal funds and $0.5 million is from increased rebates from drug manufacturers.

Breast Cancer Early Detection Program

This tobacco tax funded program provides breast cancer screening for low-income, uninsured, and underinsured women. In addition to $2.5 million redirected in January, the May Revision includes $1.1 million to provide these services to an additional 14,000 women, reaching a total of nearly 112,000 women in the current year.

Caseload Programs

The revised estimate for total child health screens in the Child Health and Disability Prevention (CHDP) program is one percent higher than the Governor's Budget estimate. The General Fund caseload will decrease by 16,300 screens, and the average cost per screen will be lower resulting in a net savings of $1.5 million. The Cigarette and Tobacco Products Surtax Fund (CTPSF) portion of this caseload will be 28,600 higher than the fall estimate, requiring an increase of $292,000.

The average quarterly caseload for the California Children's Services Program will total 122,200 for the current year. The state/county funded (non Medi-Cal) caseload will decrease to 29,900, or 8.2 percent below the Governor's Budget estimate. Despite higher treatment and therapy costs per case, the declining caseload and lower county administration costs will produce net savings of $3.0 million General Fund.

Although the total caseload in the Genetically Handicapped Persons program will remain constant, the General Fund component will decrease 1.7 percent below the Governor's Budget estimate to 821 clients, resulting in net General Fund savings of $622,000.

BUDGET YEAR

AIDS Drug Assistance Program

An additional $19.3 million is needed to meet the projected ADAP demand for 1997-98. The continuing increase in ADAP costs results from increased program use, the demand for combination drug therapy, increased drug prices, and the addition of protease inhibitors and other new drugs to the ADAP formulary. The new funding includes $12.9 million General Fund to replace the previously proposed contribution of federal funds from Eligible Metropolitan Agencies. This change will allow increased Ryan White CARE Act Title I funds to be used for HIV/AIDS patient services at the local level. Additional federal grant funds and increased drug manufacturer rebates are also included. Additionally, $6.3 million will be met with cost savings anticipated from the department's shift to uniform distribution and claims processing by a statewide pharmacy benefits management contract.

Caseload Programs

The revised estimate for total screens provided by the Child Health and Disability Prevention Program is nominally higher than the Governor's Budget estimate. The General Fund supported caseload will decrease by 15,000 child health screens and the lower average cost per screen will result in a reduction of $2.9 million. The caseload supported by the Cigarette and Tobacco Products Surtax Fund-Unallocated Account, comprised typically of older children, will increase by 17,100 screens, but with lower per screen costs, a net caseload cost reduction of $1.2 million results. These amounts reflect reduced costs for the expanded vaccine program because the federal government has expanded the Vaccines for Children Program. This will reduce costs by $1.6 million General Fund and $1.2 million from tobacco tax funds.

The total average quarterly caseload in the California Children's Services program is estimated at 123,300 with a decrease in the state/county-funded (non-Medi-Cal) caseload to 26,700, or 9.9 percent below the Governor's Budget estimate. The reduced caseload and lower county administration costs will more than offset slightly higher costs per case, resulting in a net decrease of $3.2 million General Fund.

The total Genetically Handicapped Persons Program caseload is expected to decrease 2.1 percent to 790 General Fund clients compared to a 1.1 percent increase in Medi-Cal caseload. The reduced caseload and lower costs per case will reduce General Fund costs by $954,000.

Cigarette and Tobacco Products Surtax Fund-Proposition 99 Tobacco Tax

The May Revision projects only a slight overall change in Proposition 99 revenues as one-time tax collections increase current year Proposition 99 revenues by $4 million, offset by $5 million less budget year revenue. The first phase of the *American Lung Association and Americans for Nonsmokers' Rights v. State* litigation is now final and makes available previously restricted reserves of $29.7 million from the Health Education Account and $10.3 million from the Research Account. The May Revision proposes to allocate these funds to health education and research programs focused on reducing tobacco use, particularly among youth and young adults.

Department of Health Services. $29.7 million from Health Education Account reserves is proposed to support a balanced expansion of anti-smoking and tobacco education programs; $9.7 million each for the media campaign, competitive local grant projects and local public health allocations, and $600,000 for program evaluation.

University of California. $10.3 million from Research Account reserves is proposed for the University's program of applied research on tobacco use with an emphasis on youth and young adults.

The May Revision also reflects the following adjustments to programs supported by the CTPSF:

Managed Risk Medical Insurance Board. Lower-than-anticipated caseload demand in the Access for Infants and Mothers Program results in a total reduction of $2.0 million from the Hospital Services, Physician Services, and Unallocated Accounts.

Habitat Conservation Fund. An additional $2.1 million is proposed to be transferred, in lieu of General Fund, from the Unallocated Account to the Habitat Conservation Fund in order to provide the full $30 million allocation required for this fund by the Mountain Lion Initiative, Proposition 117.

DEPARTMENT OF DEVELOPMENTAL SERVICES

1996-97 No Change
1997-98 -$20.5 million

In 1997-98, funding for the developmental centers is projected to increase by approximately $2.1 million to serve 250 more clients than reflected in the Governor's Budget. The total year-end population for 1997-98 is projected to decline to 3,612 clients, rather than the 3,362 projected in the Governor's Budget.

The regional center population is projected to increase by 460 clients. While there is an overall increase projected in the population, the number of placements from the developmental centers has decreased, with a resulting reduction in high cost placements associated with these clients. Therefore, regional center costs are projected to decrease by $9.2 million. Consistent with federal welfare reform, DDS will eliminate regional center services to illegal immigrants except for those exempted at the discretion of the U.S. Attorney General based on public safety and life and safety considerations. Additionally, based on correspondence from the Federal Department of Education, the Early Start Program, as an educational program, is exempted. The reduction in costs resulting from eliminating services to illegal immigrants is $13.4 million.

DEPARTMENT OF REHABILITATION

1996-97 $ 0.7 million
1997-98 $ 3.4 million

In 1996-97, the Budget reflects an increase of 309 clients in the Habilitation Program and a decrease of 237 clients in the Vocational Rehabilitation Program for a net increase in General Fund costs of $726,000.

In 1997-98, the Habilitation Services Program is expected to serve 810 clients more than estimated in the Governor's Budget, at a cost of $4.1 million General Fund. This Program provides work activity and supported employment services to adults whose disabilities are too severe to benefit from vocational rehabilitation services. The increase is due, in part, to fewer clients transitioning into the Vocational Rehabilitation Program and new referrals from the regional centers. The Vocational Rehabilitation Program is estimated to decrease by 634 clients, resulting in General Fund savings of $758,000.

DEPARTMENT OF MENTAL HEALTH

1996-97 No Change
1997-98 $8.6 million

In 1997-98, the judicial and penal code commitments to the state hospitals are projected to decrease by 25 clients from the population reflected in the 1997-98 Governor's Budget. Additionally, the Governor's Budget projected a developmentally disabled forensic patient population of 165. However, new estimates indicate that 50 of these patients will now be served by the state developmental centers. This reduced population projection results in a decrease of $793,000 General Fund.

The Department of Mental Health is responsible for screening, evaluating and testifying in the civil commitment trial for inmates referred as potential Sexually Violent Predators (SVPs) from the California Department of Corrections. Program costs are increasing due to the courts requiring the evaluator to testify at the probable cause hearing as well as the trial. Consequently, costs for this Program are projected to increase by $2.4 million General Fund.

The 1997-98 projected population for the Conditional Release Program is 35 clients lower than reflected in the Governor's Budget, resulting in a General Fund savings of $736,000. These savings are offset by a cost of $263,000 to purchase eight beds from the forensic Institute for Mental Disease (IMD). The IMD transitions conditional release clients from the state hospital into the community and provides services to clients who are failing in the community and need to be returned for short-term placement.

Funding for outpatient mental health managed care will decrease by $6.2 million, reflecting a reduction in the growth rate of Medi-Cal eligibles, an increase in the prepaid health plan enrollees transferring into managed care, and changing the implementation date from July 1, 1997 to October 1, 1997. Funding for inpatient mental health managed care will decrease by $5.4 million, reflecting a reduction in the growth rate of Medi-Cal eligibles, a reduction in the prepaid health plan enrollees transferring into managed care and a decrease in the medical cost factor.

The May Revision also includes $19.1 million to reimburse local agencies for costs related to providing mental health services to severely, emotionally disturbed (SED) children.

DEPARTMENT OF SOCIAL SERVICES

1996-97 -$59.9 million
1997-98 -$158.2 million

Compared to the Governor's Budget, 1996-97 General Fund local assistance expenditures for the Department of Social Services are estimated to decline to $6,058.9 million, a $59.9 million reduction. For 1997-98, the estimated General Fund cost has declined by $158.2 million since January, to a revised total of $5,496.3 million. Caseload trend reductions in all major public assistance programs except In-Home Supportive Services (IHSS) contribute toward these projected savings. The $3.7 billion federal Temporary Assistance for Needy Families (TANF) block grant continues to be fully budgeted, and California's $2.9 billion TANF maintenance-of-effort requirement continues to be met. Significant augmentations to support successful implementation of welfare reform through the California Temporary Assistance Program (CalTAP) are proposed for child care and employment services and training. The May Revision also assumes that the final federal budget will restore Supplemental Security Income, consequently, General Fund spending to continue State Supplemental Payment (SSP) and IHSS benefits for legal immigrants is restored. Major program caseload changes are as follows:

AID TO FAMILIES WITH DEPENDENT CHILDREN/TEMPORARY ASSISTANCE FOR NEEDY FAMILIES (AFDC/TANF)

For 1996-97, the number of families receiving AFDC is expected to be 838,000, a decrease of 7.2 percent from the 1995-96 level. For 1997-98, the caseload is forecast to be 748,000, a 10.7-percent decline from the currently projected 1996-97 figure. The budget year caseload change is comprised of a decrease in the AFDC-Unemployed caseload of 14.1 percent compared to 1996-97, while the AFDC-Family Group caseload is expected to decline by 10 percent.

General Fund spending for the traditional AFDC program components will be $2,205.0 million in 1996-97 and $1,685.6 million in 1997-98. These amounts are $23.7 million and $280.1 million below the January budget, respectively. The following table displays AFDC/TANF spending inclusive of all program areas at the Department of Social Services:

FIGURE HW-1

1997-98 AFDC/TANF
(Dollars in Millions)

	AFDC/CalTAP		TANF Expenditures	
	January	May	January	May
Caseload	875,000	748,000		
TANF Block Grant Expenditures	$3,734.0	$3,719.0	$3,734.0	$3,719.0
General Fund, Includes All Except New Education Spending	$2,745.6	$2,533.1		
New Education Spending	$71.9	$147.9		
County Funds	$250.5	$233.5		
Total AFDC/CalTAP	**$6,802.0**	**$6,633.5**		
TANF-Funded Child Welfare Services	—	—	—	$47.5
Total TANF Expenditures			**$3,734.0**	**$3,766.5**

In January, the Budget proposed a balanced approach to using additional federal funding made available to California in the TANF block grant and in the use of state savings made available from continuing state reforms. This approach included investments in employment programs for recipients ($79.6 million), a GAIN Program expansion ($60 million in 1996-97 continued in 1997-98), training of county welfare program staff ($79.4 million), temporary continuation of the child support disregard ($40.7 million) and other miscellaneous expenditures. Additionally, TANF funding was proposed for juvenile probation placement costs ($140.9 million) and to replace $562 million of General Fund ($274 million in 1996-97 and $288 million in 1997-98) in the program. This General Fund was made available for other high-priority General Fund needs.

Major changes proposed in the May Revision of the Governor's Budget include:

- $213.1 million TANF funding for child care program expansions, including non-center based child care options for TANF families.
- $40 million TANF funding for a new employment and training services program for noncustodial parents of children who are receiving AFDC.
- $18.1 million TANF funding for the Employment Development Department to further expand the job bank automation system to include entry-level jobs to install computers in lobbies of county welfare offices for welfare clients to directly access job listings, and to fund additional county staff to assist clients in job search.
- The Department of Education's budget also is being augmented by $64 million, General Fund, for state preschool, School-Age Parenting and Infant Development, and general child care services for children up to age three. Of the $64 million, it is estimated that at least $16 million will be used to serve TANF-eligible families. Within the $475.3 million budget for Adult Education, $50 million is proposed to be targeted to serve TANF recipients. A General Fund augmentation of $10 million for the Community Colleges' Work-Study Program for TANF eligibles also is proposed. These changes total a $76 million increase for TANF eligibles.

The May Revision proposes the use of $33 million additional TANF for juvenile probation placement costs and a comparable General Fund offset in the California Youth Authority budget, a $47.5 million TANF transfer to the Social Services block grant to offset General Fund program costs in Child Welfare Services, and TANF replacement of $521.8 million, compared to $562.1 million in January, ($233.5 million in 1996-97 plus $288.3 million in 1997-98) of General Fund costs in the AFDC/TANF Program.

COUNTY ADMINISTRATION

The General Fund cost of administering county welfare programs is expected to decrease by $8.1 million in 1996-97, primarily as the result of the decreased AFDC/TANF caseload. While 1997-98 expenditures will rise by $9.9 million compared to January, spring Finance Letters related to automation projects represented an $18.6 million increase. Therefore, the May Revision increment of change for 1997-98 is a decline of $8.7 million.

STATEWIDE AUTOMATED CHILD SUPPORT SYSTEM (SACSS)

The May Revision proposes no change in funding for the Statewide Automated Child Support System (SACSS). Funding of $79.6 million ($7.7 million General Fund) in 1996-97 and funding of $84.7 million ($25.1 million General Fund) in 1997-98 is proposed to be maintained until the vendor corrects identified system defects. It will not be known until early June if these corrections will meet established quality criteria for further SACSS implementation, nor the number of counties which will continue with SACSS. In the interim, the Administration will continue to work with counties and the Legislature to complete statewide child support automation and to stabilize and provide essential support to the 22 counties currently electing to remain in SACSS.

CHILDREN'S PROGRAMS

CHILD WELFARE SERVICES

The May Revision reflects a General Fund cost reduction of $0.7 million in 1996-97 and $22.7 million in 1997-98. The 1997-98 change is primarily the result of a $47.5 million funding shift from the General Fund to the Social Services Block Grant offset by a budget year caseload increase of seven percent resulting from rising numbers of child abuse and neglect reports and increased county maintenance and operations costs for the Child Welfare Services/Case Management System (CWS/CMS) as the system becomes fully operational. Additionally, 1997-98 revised expenditures also include savings of $5 million to reflect a change in the implementation date of the Infant Health and Protection Initiative (IHPI) home visiting pilot from July 1997 to January 1998, and an increase of $1 million to provide an in-home response within 24 hours of an at-risk infant's release from the hospital.

FOSTER CARE

The May Revision reflects a General Fund reduction of $1.0 million for 1996-97 and an increase of $18.2 million for 1997-98 for the Foster Care Program. Although caseload growth is expected to be 7.5 percent in 1996-97 and 7.9 percent in 1997-98, these net expenditure adjustments also reflect an increase in federally eligible expenditures, which offset and reduce the amount of General Fund required. Expenditures for 1997-98 also are increasing because the children entering foster care are requiring more intensive services provided in group homes.

CHILD CARE

The May Revision adds $213.1 million to the Governor's 1997-98 Budget to expand CalTAP-related child care. This increase is proposed to be funded with a transfer of TANF block grant funds to the Child Care and Development block grant in the Department of Education. These funds will be reimbursed to DSS through an interagency agreement. This increase is expected to provide sufficient resources to meet the anticipated child care demand that will result as welfare recipients prepare for and enter the work force. Funding was also increased to account for the elimination of the child care disregard on January 1, 1998 for current welfare recipients who will not transition into CalTAP program services until later in 1998, an increase in the estimated monthly cost of CalTAP child care due to revised assumptions, and a change in the CalTAP services component implementation date from April 1, 1998 to January 1, 1998.

ADULT PROGRAMS

SUPPLEMENTAL SECURITY INCOME/STATE SUPPLEMENTAL PAYMENT (SSI/SSP)

In conformity with the federal Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (HR 3734), the January budget proposal assumed General Fund savings of $153 million resulting from the elimination of SSI/SSP eligibility to noncitizens. However, based upon the assumption that the final federal budget will restore SSI benefits to legal immigrants who were in the country on or before August 22, 1996, the SSP savings will not be realized and will instead be used to continue benefits to those individuals. The May Revision reflects this restoration of benefits and will continue service for a currently estimated average monthly caseload of approximately 96,000 legal immigrants recipients who would otherwise lose their benefits commencing in August due to their naturalization status.

With legal immigrants remaining on the rolls, SSI/SSP expenditures are expected to decrease by $49.0 million in 1996-97 and increase by $64.3 million in 1997-98. SSI/SSP Program caseload is anticipated to decrease by 3.4 percent from 1996-97.

The May Revision continues to assume passage of federal legislation that would authorize 4.9-percent statewide and regional grant reductions; these savings however, have been reduced by $5.6 million based on the revised caseload estimates.

In-Home Supportive Services (IHSS)

Due to the federal budget assumption discussed above under the SSI/SSP Program, and the state law which links IHSS eligibility to SSI/SSP eligibility, the $24 million General Fund savings anticipated for 1997-98 in the January budget proposal, will not be realized due to the restoration of SSI/SSP benefits to legal immigrants. The May Revision reflects this restoration of benefits, and will continue service for an estimated 17,800 IHSS legal immigrant recipients monthly who would otherwise lose their benefits commencing in August due to their naturalization status

General Fund expenditures for the IHSS Program are expected to decrease by $2.3 million in 1996-97 and increase by $14.0 million in 1997-98. IHSS caseload is expected to increase 3.9 percent year-to-year.

The May Revision also reflects a $14.4 million reduction in IHSS General Fund expenditures due to an increase in available Federal Title XX funding.

PUBLIC SAFETY

DEPARTMENT OF CORRECTIONS

INMATE/PAROLEE POPULATION/CASELOAD CHANGES

1996-97 -$14.8 million
1997-98 -$3.7 million

CURRENT YEAR

Based on the Department of Corrections' (CDC) spring estimates and recent population trends, the May Revision reflects a June 30, 1997 population of 151,552 inmates. Although this is 582 more than reflected in the Governor's Budget, it accounts for a savings of $7.2 million. This savings is due to delayed activation of inmate emergency housing beds and a reduction in the number of individuals who attended the McGee Academy to be trained as correctional officers. The revised population estimates represent an increase of 10,535 inmates (7.5 percent) over the June 30, 1996 population level.

The projected year-end parolee population is 101,110. This is 2,272 less than the January budget and represents a savings of about $7.6 million. This savings is related primarily to delayed activation of contract beds in the community which were intended to serve parole violators who are pending revocation hearings and violators who the Board of Prison Terms determines should be returned to a confined setting for a short period of time. However, this revised parole population level is still an increase of 3,097 (3.2 percent) over June 30, 1996. The net effect of the changes noted above is a General Fund savings of $14.8 million.

BUDGET YEAR

The CDC's spring estimates combined with recent population trends reflect a June 30, 1998 population of 159,872 inmates. This is 49 more than anticipated in the January budget and an increase of 8,320 inmates (5.5 percent) over the revised June 30, 1997 population level noted above.

The projected year-end parolee population is 106,588. This is 2,694 fewer than anticipated in January. This population decline will result in delayed activation of parole violator housing. Additionally, cost savings related to a reduction in the contract costs for the Peter Pitchess Facility in Los Angeles are reflected in this program. The parolee population level projected for the budget year is an increase of 5,478 (5.4 percent) parolees over the revised population trend estimated for June 30, 1997. Although delayed, the adjustments reflect full activation of 1,400 contract beds at the Peter Pitchess Jail Facility in Los Angeles and a total of 2,000 community correctional facility beds. The net effect of these inmate and parolee adjustments is a General Fund savings of $3.7 million.

ALTERNATIVE SENTENCING (BOOT CAMP) PROGRAM

1996-97 No Change
1997-98 No Change

A recent evaluation by CDC of the Boot Camp Program indicates that the Program did not meet its stated goals. Therefore, legislation will not be sought to continue this program beyond the December 31, 1997 sunset date currently in law.

LOCAL ASSISTANCE

1996-97 No Change
1997-98 $20.1 million

An increase of $5.6 million is proposed in the budget year to allow CDC to reimburse local criminal justice agencies for charges relative to the prosecution of crimes committed in prison, sanity hearings, extradition orders, and coroner costs. This increase will address both unpaid prior year expenses as well as projected current and future year increased costs.

In addition, an increase of $14.5 million is proposed to reimburse counties for the costs of detaining parole violators in local jails pending parole revocation hearings. These funds will address projected increased costs for both the current and budget years. The combination of the adjustments noted above will provide a total increase in local assistance funding of $20.1 million.

ILLEGAL IMMIGRANT FELONS

The May Revision includes a reduction of $46.7 million in reimbursements from the Federal Government in the budget year for the costs of incarcerating and providing parole supervision for illegal immigrant felons and a corresponding increase in budget year General Fund expenditures. These adjustments are based on an expected federal appropriation for all states of $500 million in Federal Fiscal Year 1998 for the State Criminal Alien Assistance Program.

BOARD OF CORRECTIONS

JUVENILE JUSTICE REFORM

The Administration is supporting legislation to address a variety of juvenile justice reform efforts to divert first-time juvenile non-violent offenders from the criminal justice system, and to identify and prosecute gang members in an effort to foster safer communities. A total of $38.6 million is set-aside for these efforts. The following highlights the major proposals:

- Community Law Enforcement and Recovery (CLEAR) Demonstration Project—Approximately $15.1 million is included for a Los Angeles County Program which involves community-based organizations, schools, businesses and law enforcement agencies. This program is designed to identify gang members, provide targeted law enforcement efforts and intensive probation supervision. In addition, $2.4 million is proposed for a statewide effort to obtain civil injunctions against gangs that threaten, harass, and victimize communities. Funding of $300,000 will also be provided for training of district attorney office staff in gang prosecution techniques.

- Delinquent or "At-Risk" Juveniles—$20 million is included for a program for first-time juvenile non-violent offenders whose parents have voluntarily sought a petition with the court to assist in controlling a minor's behavior. Grants will be provided to counties, cities, community organizations, and non-profit agencies on a competitive bid basis for deferred entry of judgment activities and voluntary parental petition efforts. It is intended that all local programs collaborate with the county's existing Juvenile Justice Coordination Council.

DEPARTMENT OF THE YOUTH AUTHORITY

POPULATION ADJUSTMENTS

1996-97 -$0.489 million
1997-98 $0.007 million

For 1996-97, the Youth Authority's year-end institution population is projected to be 9,015, a decrease of 410 from the 9,425 projection included in the Governor's Budget. Similarly, for 1997-98, the Youth Authority projects a year-end institution population of 9,145, or 400 less than previously projected. Chapter 6, Statutes of 1996 requires counties to reimburse the State on a sliding fee scale for less serious offenders committed to the Youth Authority. The Youth Authority's population has been declining since the implementation of this new fee on January 1, 1997. For both the current and budget years, the projected population decrease has resulted in a reduction in the amount of reimbursements to be collected by the Youth Authority from counties.

For 1996-97, the Youth Authority projects a year-end parole population of 6,180, or 25 parolees less than previously projected. For 1997-98, the Youth Authority projects a year-end parole population of 5,970, or 180 less than previously projected.

To accommodate these changes in population, the following adjustments to the Governor's Budget are necessary. The 1996-97 fiscal year includes a $99,000 reduction in General Fund, a $390,000 reduction in Proposition 98-General Fund, and a $1,304,000 reduction in reimbursements. The 1997-98 fiscal year includes a $966,000 increase in General Fund, a $959,000 reduction in Proposition 98-General Fund, and a $4,082,000 reduction in reimbursements.

COUNTY ASSISTANCE FOR JUVENILE RANCHES AND CAMPS

1996-97 No Change
1997-98 -$32.7 million

The Governor's Budget included $32.7 million (General Fund) to provide support for county ranches and camps. In lieu of this appropriation, the May Revision includes an additional $32.7 million in Federal Funds (Temporary Assistance for Needy Families Block Grant) which will be allocated to counties by the Department of Social Services. The Federal Funds will continue to be allocated to counties by the Department of Social Services, using the same methodology as has been used by the Youth Authority in recent years.

EXPENDITURES

ENHANCED VICTIM SERVICES

1996-97 No change
1997-98 $5.0 million

OFFICE OF CRIMINAL JUSTICE PLANNING

The Board of Control is projecting reserves in the Restitution Fund in excess of $30 million. The Administration proposes to take advantage of this opportunity by proposing to expend a total of approximately $15 million over a three year-period to enhance the availability of victim services. It is proposed that approximately $5 million be appropriated from the Restitution Fund to the Office of Criminal Justice Planning in 1997-98, 1998-99, and 1999-2000 to fund three programs:

- **Multidisciplinary Child Sexual Abuse Advocacy** - An augmentation of $910,000 is proposed to fund 13 projects that would coordinate the efforts of members from various professional fields, including social services, medical, mental health, law enforcement, and others to provide for the child's physical needs as well as protection and intervention services. These funds would be allocated on a competitive basis.

- **Sexual Assault Response Teams** - An augmentation of $1 million is proposed to fund 17 grants that would establish new sexual assault response teams, comprised of representatives from law enforcement agencies, medical facilities, social services, and advocate agencies to provide coordinated responses to sexual assault victims. These grants would be awarded on a competitive basis.

- **Victim Advocates** - An augmentation of $2.9 million is proposed to fund 29 on-site victim advocates. This program would enable Victim-Witness centers to assign a victim advocate to selected police and sheriff departments in localities with populations exceeding 100,000. These funds would be awarded on a competitive basis.

An augmentation of $150,000 is proposed for state operations to provide 1.5 positions to administer these programs.

BOARD OF CONTROL

1996-97 No change
1997-98 $1.3 million

The Administration will be supporting actions by the Board of Control to: (1) increase the maximum allowance for funeral/burial expenses of victims of crime, which was last increased in 1990, from $3,500 to $5,000 at an estimated annual cost of $1.2 million; and (2) provide benefits to out-of-state survivors of homicide victims in California, which will bring California into conformity with the policies of most other states, at an estimated annual cost of $100,000.

DEPARTMENT OF FORESTRY AND FIRE PROTECTION (CDF)

EMERGENCY FUND AUGMENTATION

1996-97 No change
1997-98 $40.0 million

The Emergency Fund is used to cover the added costs necessary (in excess of CDF's support budget) to control wildland fires that extend beyond the initial attack phase of fire fighting. Currently, the 1997-98 budget proposes a General Fund appropriation of $20 million, with another $10 million available from the Special Fund for Economic Uncertainties upon allocation by the Director of Finance.

Historically, this annual allocation has not been sufficient to cover CDF's emergency fire suppression costs. This is evident by the fact that CDF has had to seek an annual General Fund deficiency six out of the last seven years. In order to budget at a level to more closely cover anticipated emergency fire suppression costs, and to allow the department adequate funds to ensure uninterrupted operations during the summer-fall 1997 and spring 1998 fire season, it is proposed that the Emergency Fund appropriation be increased to $60 million.

FIGURE PS-1

CDF Emergency Fund Expenditures
(Dollars in Thousands)

Fiscal Year	Total	General Fund (Budgeted)	General Fund (Augmented)	Federal Fund	Reimbursed
1997-98	$24,000*	$20,000*	—	$4,000	$0
1996-97	117,000	30,000	$69,000	10,000	8,000
1995-96	60,423	30,000	25,978	4,445	0
1994-95	69,858	24,992	30,866	14,000	0
1993-94	65,679	30,000	6,530	1,582	27,567
1992-93	85,591	30,000	26,858	4,700	24,033
1991-92	22,524	19,934	0	2,000	590
1990-91	70,825	10,000	52,897	7,928	0

* Another $10 million (from the General Fund reserve) is available upon allocation by the Director of Finance (provisional language in CDF's budget).

General Government

California Infrastructure and Economic Development Bank

1996-97 No change
1997-98 $50.0 million

The Infrastructure Bank, which was established in statute by Chapters 94 and 749 of 1994, is proposed to be initially capitalized by a transfer of $50 million from the General Fund to the California Infrastructure and Economic Development Bank Fund. The purpose of the Bank is to enhance economic development by providing or assisting in financing of a broad range of public infrastructure projects which support private economic expansion. By using the funds to guarantee loans or provide other credit enhancements, the funds are expected to leverage private capital.

Office of Emergency Services (OES)

1996-97 No change
1997-98 $20.1 million

Northridge Earthquake/Other Disasters—The Governor's Budget included $55.6 million for payment of the non-federal share of local government claims during the current year, and $59.2 million for payment of such claims in 1997-98. The May Revision reflects a $20.1 million General Fund budget year augmentation to the Local Assistance item. Of this amount, $15.1 million is for projected increases in the non-federal share of City of Los Angeles Northridge Earthquake claims, which are expected to become eligible for payment during 1997-98. The remaining $5.0 million is for the State's share of claims for disasters other than the Northridge or the Loma Prieta earthquakes, and is attributable to increased payments for the January 1997 floods and storms, various previous disasters, and expected decreases in payments for the March 1995 winter storms.

1997 Storms/Floods

In the aftermath of major disasters in recent years, the Administration has agreed to legislation which would provide additional tax relief to victims, to offset the impact of disasters on local property tax revenues, and to authorize the State to fund the local share of disaster-related costs approved by the Federal Emergency Management Agency (FEMA). The May Revision assumes that legislation will be enacted regarding the storms and flooding which occurred earlier this year and funding necessary for these programs is included in the General Fund reserve.

After previous disasters, the Administration has agreed to additional income tax relief for flood victims beyond current law (allowing casualty losses to be carried forward). Casualty loss legislation, as approved after previous disasters, would reduce General Fund revenues approximately $5.0 million in 1997-98. The State has also offset the impact of disasters on local property tax revenues. Funding local property tax losses is estimated to cost $0.5 million in 1996-97, and an additional $1.0 million in 1997-98. In addition, the State has generally agreed to legislation authorizing the funding of the entire non-federal share of FEMA-approved local disaster claims. Without such legislation, local agencies are required to fund 25 percent of the 25-percent non-federal share of FEMA-approved costs (6.25 percent of total costs). Funding the entire non-federal share of FEMA-approved costs would increase General Fund expenditures by an estimated $1.6 million in 1996 97, and $3.3 million in 1997-98.

DEFICIENCIES IN MANDATE APPROPRIATIONS

1996-97 No change
1997-98 Non-Proposition 98 $60.2 million
Proposition 98 ($191.0 million)

The State Controller's Office (SCO) has reported that the claims they received from local governments for reimbursement of state-mandated local costs, which are payable from the last three Budget Acts and the last two mandates claims bills, exceeded the appropriations therein by $251.2 million. Of this amount, $191.0 million represents claims from local educational agencies which count toward the Proposition 98 funding guarantee. Funding for this shortfall is addressed in the Education section. The balance of $60.2 million represents claims from other local governmental agencies (cities, counties, and special districts). Although most of these claims have not been audited at this time, the SCO reported the total amount claimed because of legislation enacted last year, which requires the payment of interest on claims which are not paid within specified timeframes.

Based on the SCO's recent experience in auditing such claims, the amounts ultimately disallowed as the result of their audits should exceed any interest which accrues; on that basis, no additional funding for interest is included in this proposal.

MOTOR VEHICLE ACCOUNT FUND BALANCE

The Governor's Budget contained several actions necessary to bring the Motor Vehicle Account (MVA) into balance, including a $51 million proposal to increase various driver-related fees and a shift in costs to the State Highway Account of $31.8 million. The Budget also contained an assumption that $40 million in Public Employees Retirement System (PERS) surplus assets in the California Highway Patrol (CHP) account would be available to offset employer and employee contributions owed by the CHP in both the current and budget years.

Based upon recent discussions with the actuarial staff at PERS, no new surplus will be posted to the CHP Surplus Assets Account. The result is that the MVA will be out of balance in the current year by $22.2 million, and by $18.9 million in the budget year.

Due in part to the loss of the anticipated PERS surplus assets funding, the original budget proposal has been revised. The new proposal will balance the MVA in the current year, and produce an estimated reserve of $34 million for the budget year. Specifically, the Administration is proposing the following actions to bring the MVA into balance:

REVENUES

- Delete all provisions of the Administration's January proposal to increase various driver's related fees, and instead substitute a $1.00 increase in the vehicle registration fee and a $5.00 increase from $10.00 to $15.00 in the vehicle transfer fee. A $1.00 vehicle registration fee increase is estimated to produce $19 million in new revenues to the MVA in fiscal year 1997-98. The vehicle transfer fee increase is estimated to produce $19 million annually.

- Fees for the reissuance of licenses which have been suspended or revoked will be increased administratively to a level consistent with the actual cost of issuing those licenses. This is estimated to raise approximately $16 million in revenues.

CALIFORNIA HIGHWAY PATROL

- Continue the Administration's January budget proposal to fully shift the costs of the Commercial Vehicle Inspection Program operated by the CHP to the State Highway Account. This results in a savings of $31.8 million to the MVA.

- Increase the current year loan from the State Highway Account by $22.2 million to a total of $35 million, and provide that this loan be repaid over the subsequent two fiscal years with the amount of repayment in fiscal years 1997-98 and 1998-99 to be determined by the Director of Finance. Any repayment in 1997-98 will reduce the projected $34 million State Highway Account balance.

AIR RESOURCES BOARD

- Permanently eliminate $26.7 million in funding from the MVA supporting the stationary source program in the Air Resources Board (ARB) support and local assistance budgets, and replace these funds with the same amount from the General Fund.

TAX RELIEF

HOMEOWNERS' PROPERTY TAX RELIEF PROGRAM

1996-97 -$13.9 million
1997-98 -$14.6 million

The California Constitution exempts homeowners from paying property taxes on the first $7,000 of the assessed value of their principal place of residence. The Constitution requires the State to reimburse revenues lost due to this exemption.

For the current year, it is estimated that the county claims for the Homeowners' Property Tax Relief Program will total $383.3 million; $13.9 million lower than the estimated $397.2 million General Fund expenditures in the Budget Act. This means that approximately 181,000 fewer homeowners claimed this benefit in 1996-97. The May Revision proposes to reduce the Program's 1997-98 level of $405.5 million by $14.6 million to $390.9 million. The Homeowners' Property Tax Relief Program will continue to reflect a two-percent increase in fiscal year 1997-98, over the 1996-97 revised cost.

LOCAL GOVERNMENT FISCAL RELIEF

As part of the May Revision, the Administration is proposing to return $100.0 million of the base of the property tax transfer to counties, cities, and special districts. The Administration will support legislation to accomplish this transfer which must take into account the additional resources made available to counties and cities through Proposition 172.

STATE RETIREMENT CONTRIBUTIONS

1996-97 $ 0.2 million
1997-98 $ 2.7 million

The May Revision reflects a General Fund increase from the Governor's Budget of $0.2 million in 1996-97, and $2.7 million in 1997-98:

- **State Teachers' Retirement System (STRS)**—General Fund contributions to STRS will increase by $11.0 million for 1997-98 (from $925.5 million to $936.5 million). This is due to increases in teacher salaries and new hires which are the basis for the statutory formula.

- **Legislature Retirement System (LRS)**—General Fund contributions will increase by $0.2 million in both 1996-97 and 1997-98 (from $0.5 million to $0.7 million).

- **Public Employees' Retirement System (PERS)**—The State's 1997-98 General Fund obligation to the PERS is estimated to decrease by $7.0 million from the Governor's Budget due to favorable economic factors (from $680.0 million to $673.0 million). Pursuant to current law, the 1997-98 General Fund obligation to PERS will not be paid until 1999-2000 and, therefore, would have no effect on 1997-98 budget totals.

- **Surplus Account**—PERS reports that $8.5 million in State surplus assets is available to offset General Fund payments. Pursuant to Control Section 3.60(b) of the Budget Act, the $8.5 million state surplus assets will be used to reduce the July 1, 1997 General Fund payment to PERS (from $587.5 million to $579.0 million).

PAYMENT OF INTEREST ON GENERAL FUND LOANS

1996-97 -$41.0 million
1997-98 -$38.5 million

For 1996-97, the Governor's Budget anticipated the cost of interest on General Fund loans for internal borrowing to be $51.0 million. The interest costs are now estimated to be approximately $10.0 million, or a savings of $41.0 million. This is based on actual disbursements of approximately $9.3 million through April 30th and anticipated costs through the end of the fiscal year. Given the higher revenue flow, as well as the historical trend from last year, it is not anticipated that the State will incur any significant additional interest cost for the balance of the current year. The interest cost for external borrowing was anticipated at $117 million. This estimate remains the same.

For 1997-98, interest costs on internal borrowing was also anticipated to be $51.0 million. These costs are now estimated to be approximately $20.0 million, or a savings of $31.0 million. These savings are based on revised anticipated revenues and expenditures for 1997-98. The Governor's Budget also estimated the sale of a Revenue Anticipation Note (RAN) in the amount of $3.0 billion in July 1997, with an interest rate of 5.0 percent. This equates to an interest cost of $150.0 million. Based on current market conditions, the interest rate on the RAN is now anticipated to be 4.75 percent. This would result in a savings of $7.5 million in the budget year.

GENERAL OBLIGATION BONDS AND COMMERCIAL PAPER DEBT SERVICE

1996-97 -$ 7.9 million
1997-98 -$70.3 million

The proposed 1997-98 Governor's Budget anticipated current year General Obligation (G.O.) bond debt service expenditures of approximately $1.953 billion, and budget year expenditures of approximately $1.979 billion.

Due to revisions in the State Treasurer's Sales Plan, a lower-than-estimated G.O. bond issue in March 1997 and a lower interest rate for this sale, expenditures are estimated to decrease by $7.9 million in the current year, and by $70.3 million in the budget year. The total effect over the two years is a decrease of $78.2 million.

LEASE-REVENUE BOND DEBT SERVICE PAYMENTS

1996-97 -$2.7 million
1997-98 -$42.0 million

The Governor's Budget anticipated current year General Fund debt service and related costs for lease-revenue bonds of $383.7 million and budget year expenditures of $394.3 million.

Due to refundings, availability of bond fund surpluses and master reserve account adjustments, General Fund expenditures for this debt service and related costs can be reduced by $2.7 million in 1996-97, and $42.0 million in 1997-98. The net effect over the two years is a savings of $44.7 million.

1997-98 STATE APPROPRIATIONS LIMIT CALCULATION

Pursuant to Article XIIIB of the California Constitution, the 1997-98 State Appropriations Limit (SAL) is estimated to be $44.711 billion. The revised limit is the result of applying a growth factor of 6.45 percent. The revised 1997-98 limit is $416 million below the $45.127 billion estimated for 1997-98 in January. This decrease is due to changes in the following factors:

	January Percentage	May Revision Percentage
Per Capita Personal Income	5.34	4.67
State Civilian Population	1.76	1.35
K-14 Average Daily Attendance	2.35	2.20

The SAL for 1996-97 does not change since it was statutorily determined by Section 12.00 of the 1996 Budget Act.

The proposed 1997-98 appropriations subject to limitation are more than $7 billion under the limit.

General Fund
Revenues and Expenditures
(Dollars in Billions)

	Revenues	Expenditures
1991-92	$42.0	$43.3
1992-93	$40.9	$40.9
1993-94	$40.0	$39.0
1994-95	$42.7	$42.0
1995-96	$46.3	$45.4
1996-97	$49.4	$49.2
1997-98	$52.0	$51.7

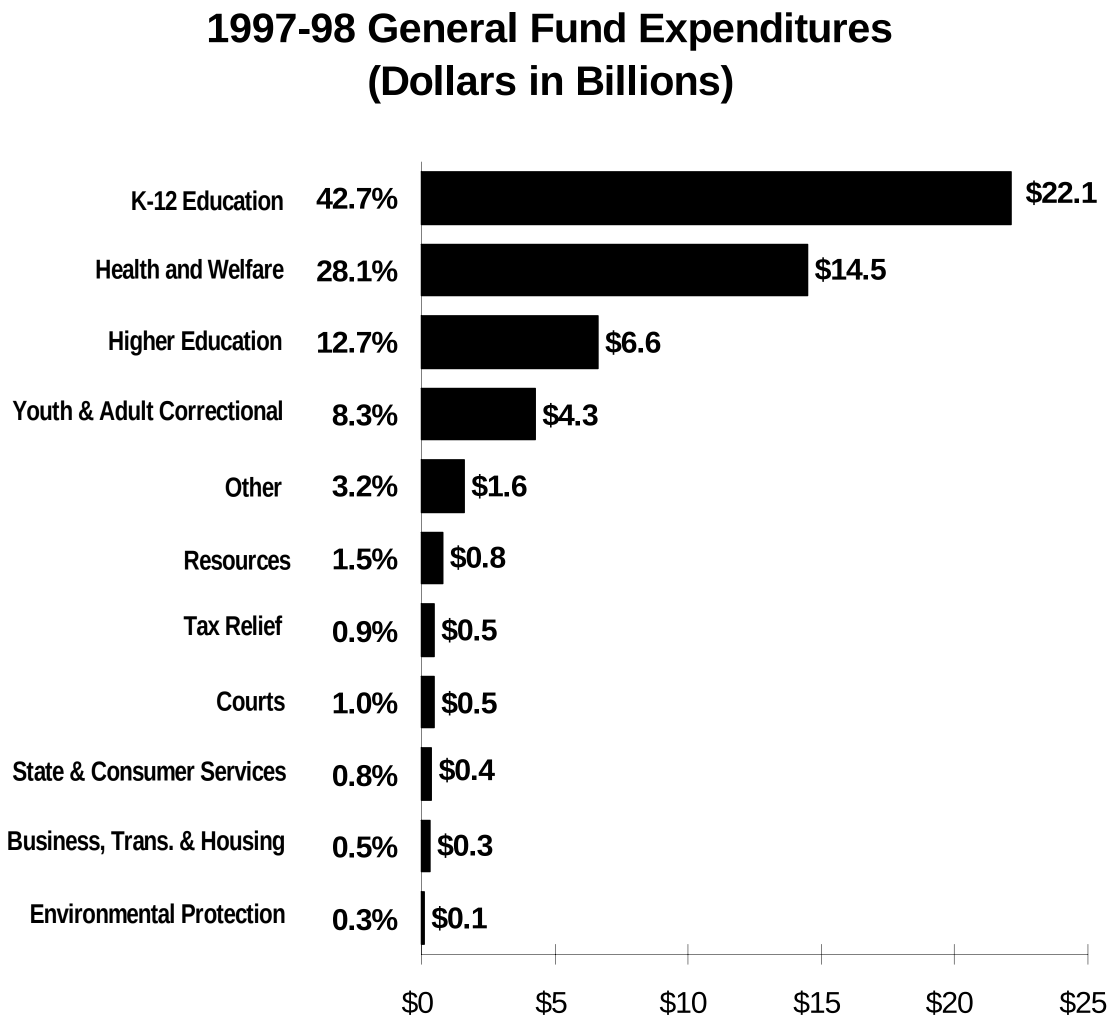
General Fund
Budget Summary
(Dollars in Millions)

	1996-97	1997-98
Prior Year Balance	$564	$763
Revenues and Transfers	$49,365	$51,960
Total Resources Available	$49,929	$52,723
Expenditures	$49,166	$51,692
Fund Balance	$763	$1,031
Budget Reserves:		
Special Fund for Economic Uncertainties	312	580
Reserve for Liquidation of Encumbrances	451	451

General Fund Expenditures by Agency

(Dollars in Millions)

	1996-97	1997-98
Legislative, Judicial, Executive	$1,575	$1,416
State and Consumer Services	376	394
Business, Transportation & Housing	300	260
Trade and Commerce	49	98
Resources	832	782
Environmental Protection	91	150
Health and Welfare	14,784	14,551
Youth and Adult Correctional	3,822	4,300
K-12 Education	20,182	22,082
Higher Education	6,202	6,589
General Government	953	1,070
Total	**$49,166**	**$51,692**
January Totals	$48,443	$50,301
Change from January	$723	$1,391
Percent Change from January	1.49%	2.77%


1997-98 General Fund Expenditures
(Dollars in Billions)
K-12 Education 42.7% $22.1
Health and Welfare 28.1% $14.5
Higher Education 12.7% $6.6
Youth & Adult Correctional 8.3% $4.3
Other 3.2% $1.6
Resources 1.5% $0.8
Tax Relief 0.9% $0.5
Courts 1.0% $0.5
State & Consumer Services 0.8% $0.4
Business, Trans. & Housing 0.5% $0.3
Environmental Protection 0.3% $0.1
$0
$5
$10
$15
$20
$25

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Budget Program Areas

Budget Planning and Preparation, Cash Management, Statewide Issues	Carl Rogers	445-5332
Education	Kathryn Gaither	445-0328
Health and Welfare	Stan Cubanski	445-6423
Revenue Forecasting, Economic Projections, Demographic Research, Business, Transportation and Housing, and Trade and Commerce	Wallis Clark	322-2263
Youth and Adult Correctional, Justice, General Government and State and Consumer Services	Calvin Smith	445-8913
Resources, Environment, Energy, Capital Outlay and Legislation	Fred Klass	324-0043
Employee Relations, Retirement Systems	Robert Straight	327-0201

* Judicial and Local Government

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